

# Diversification of Your Operation, How

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Introduction .....	1
The Steps involved .....	1
Conduct a SWOT Analysis .....	2
Research the Outcome .....	2
Develop a Business and Marketing Plan .....	3
Approach your Lender, if Needed .....	4
Implement the Plan .....	5
Evaluate the Practice .....	5
Adjust the Plan and Practice .....	5
Summary.....	5

## Introduction

If you are considering diversifying your farm or ranch business, there are several steps you should follow to fully evaluate your options before the introduction of the new enterprises. Diversification should not be entered into lightly, but with much thought and planning. Diversification may require additional land, labor, and capital, so approach the planning process carefully. The goal of diversification is to protect you against downside risk with its associated cash flow problems and help you better utilize your land, labor, and capital.

## The Steps Involved

Once you decide to diversify your business, there are many steps involved before, during, and after beginning the new enterprise. If your operation is not diversified, collecting and assessing data for your analysis may take a year or more. The steps involved in evaluating and implementing diversification opportunities are:

- Conduct a SWOT analysis.
- Conduct additional research based on the outcome of the SWOT analysis.
- Develop a business plan, including a marketing plan.
- Evaluate the feasibility of the plan, taking into account your availability of land, labor, and capital, and make changes if needed.
- Approach your lender, if needed.
- Implement the plan.
- Evaluate the impact of your diversification plan on farm income and farm resources.
- Adjust the plan and practice, if needed.

If you follow these steps, you will have a greater chance of success in the new enterprise you have chosen. You do not want to invest savings or capital into an unsuccessful enterprise. These steps may also save you from investing in something that may not have history of profitability.

### **Conduct a SWOT Analysis**

SWOT is an acronym for **S**trengths, **W**eaknesses, **O**pportunities, and **T**hreats. This procedure should include input by all people involved in the diversification decision including family members, employees, and the business management support team. During this initial analysis process, no ideas or opinions should be discarded without much thought and consideration.

Strengths are mostly internal and are skills and resources that family members, employees, and the business team bring to the business. If one person has mechanical abilities and has experience with your equipment, this is considered a strength within this analysis. Strengths are used to combat weaknesses within your operation.

Weaknesses are also mostly internal to your business and consist of skills or resources that may be lacking within the operation. Lack of skill in handling business records and filing necessary tax forms would be a weakness. Having an accountant as part of your business team would be a potential method of combating this weakness and a way to turn a potential problem into a strength. Many such weaknesses can be overcome by hiring someone with the expertise or experience the business lacks.

Opportunities are mostly external and exist in the world surrounding the business. For example; if you are considering an on-farm market, owning land adjacent to a well traveled road is an opportunity. You have the opportunity to place your market or stand in a place that has adequate traffic to sustain the market. Having to purchase suitable land in this example is a weakness or threat. You may have to seek outside opinions to determine all of your opportunities.

Threats are also mostly external and are from outside of your direct control. Using the previous example; a neighboring farm stand one mile away from your proposed market is a potential threat. You cannot control what your neighbor does with their land, so you may need to consider another option unless you are selling different products.

Based on a SWOT analysis, you will determine if further research into your potential diversification opportunity is warranted. One potential conclusion is that you decide that the opportunity is not feasible for your business. This is a common conclusion in the business world and you should not think of it as a failure. By doing an honest job in evaluating your business, you can avoid costly mistakes. Businesses often revisit their past SWOT analyses and business plans to see if conditions have changed to warrant further consideration.

## **Research the Outcome**

Once you have chosen a potential enterprise and completed the SWOT analysis, you will need to begin the research process. This research will also be used when you write your business plan. There are many places to find information. These include but are not limited to:

- libraries.
- books and magazines.
- the Internet.
- your extension service.
- trade associations.
- friends and neighbors.

Finding information is critical concerning the past and present performance of the industry and its future prospects. You will need to use as many sources as possible to confirm what you discover from each source. Do not use any information without confirmation from another source if possible. If someone tells you about a once in a lifetime opportunity or a can't miss product, having confirmation from other reliable sources is critical.

In any industry there is a period of early adoption where the industry is rapidly growing. There is then a mature stage where growth slows or plateaus, often followed by a decline in the industry. During the time when there are only a few suppliers of a product, the price of the product usually increases. Once the market becomes adequately supplied, price competition usually ensues. If the market becomes saturated with the product, the price will decline. All industries constantly research new products and production technologies to try to gain a competitive advantage. Being an early adopter who provides a highly demanded product is an enviable position. Competitive advantages can also be gained by producing traditional products at lower cost or in ways that add value for the consumer. Adding value for the consumer by providing new varieties or such attributes as "locally-grown", "farm fresh", and "organic" are ways which farmers can benefit from diversification. Regardless of whether you are launching a new product or trying to improve on an existing one, you can not make a good business decision without adequate research.

## **Develop a Business and Marketing Plan**

There are many resources to help you write your business plan. This topic is covered by many sources and there are companies who will write the plan for you for a fee. The advantage to writing the plan yourself is that it makes it your own. Providing someone else with information and paying them to write the plan is not as personal as writing it yourself. Do not worry about having perfect grammar or punctuation; your lender will realize that you are serious about the enterprise if you write the business and marketing plan yourself. You will use the research you conducted after the SWOT analysis as the foundation for your business plan. You will need to include up-to-date financial information as this is

an important part any lender will require. The format of the business plan should be:

- Title page.
- Table of contents
- Executive summary
- Mission, goals, and objectives.
- Background information.
- Organizational structure.
- Marketing plan.
- Financial statements and projections.

The title page should be as attractive as you can make it. It should contain the name of the operation or proposed enterprise and the owner's name and address.

The table of contents will help the reader find specific sections so your plan will need to have page numbers. The section titles and page number of the beginning of the section should be included in the table of contents.

The executive summary is the last section of the plan you will write, but it is found at the beginning of the plan. The executive summary will tell the reader the basic components of the plan and contains a brief summary of the industry and financial documents you include in the plan. It should contain the basic conclusions of the analysis and highlight the most important findings, including a brief listing of strengths and weaknesses. This is the most read portion of a business plan.

The mission, goals, and objectives tell the reader what the owner(s) and business team feel are important attributes of the operation. It will contain the mission statement, the goals of the business, and how these goals will be achieved. It will give the reader insight into the character of the business owners, the industry in which it operates, and its business support team.

The background information will support your conclusions in the executive summary. This information is derived from your research. This section is usually the longest in the plan. You want to include as many details as possible to support your final decision.

The organizational structure section contains discussion of the business structure and the members of the business team. Describing the current structure and any changes needed in order to adopt the enterprise should be detailed in this section. Discussing appropriate risk management strategies or business succession planning issues would also be appropriate in this section. The marketing plan will tell the reader how the product will be marketed. You should describe your pricing strategy, advertising methods, and the target marketing population. Again, your previous research will be critical to complete

this section. All expenses associated with advertising and marketing should be supported within this section so the reader will understand your strategies.

The financial plans should contain as much detail as possible. These plans should include a balance sheet, income statement, and cash flow projections. The balance sheet will be developed from the current business to show the health of the business. The income statement should show the projected income and expenses for each month and be constructed for either a twelve month period or a complete production cycle (whichever makes more sense). A cash flow budget will show when additional funds are needed and how any loans will be paid.

Once you have conducted your SWOT analysis, conducted the necessary research, and written the business and marketing plan, you are ready to evaluate the plan. If you have determined that you have a viable enterprise, you then write the executive summary including your recommendations for the enterprise.

### **Approach your Lender, if Needed**

If your proposed enterprise is viable, it is generally pretty obvious whether you have adequate capital to fund the diversification or need outside funding. If outside funding is needed, take your business plan to your lender (or investors). A well-prepared business plan will make a favorable impression on your lender and will greatly facilitate their evaluation process. As always, make an appointment and dress appropriately. Be polite, professional, and truthful in all dealings with any loan officer as they will be making the lending recommendation to the institution.

If you do not currently have a lending institution, find one that is familiar with the enterprise you propose. Take any supporting documents you feel necessary and if you are approaching a new institution or lender, they will probably request several years of tax returns.

### **Implement the Plan**

Once you have secured sufficient capital, you are ready to put your business plan into practice. Start slowly and try to anticipate and problems before they arise. Keep records on all aspects of the business, from financial information to a log of all activities. You will need to constantly evaluate the new enterprise to determine where you can improve and ensure yourself of continued success. If you encounter minor problems, your records should help determine where adjustments should be made.

### **Evaluate the Practice**

Constant evaluation of any new enterprise is essential. If the enterprise is something completely new to the business, you may ask others for advice about the health of the enterprise. Your accountant will be very helpful for this task. At the beginning of any new enterprise, monthly (or more frequent) meetings with

your business team may be necessary. Make sure everyone knows about any unusual happenings within the business. Constant evaluation of your risk management plan is also recommended so any adjustments in insurance coverage or marketing practices can be made quickly.

### **Adjust the Plan and Practice**

You may find that after the initial year or season of the enterprise that you may need to make adjustments. You may need to either expand or contract the scale of the enterprise depending on your experiences. This is not uncommon because you have gained valuable experience and have a better working knowledge than you had initially.

### **Summary**

No one can guarantee success for a new enterprise. By following the steps outlined here, you will have a better chance of success than someone who does not. By investing time in the planning process, you can avoid many pitfalls you would overlook otherwise. Good planning is often the difference between operating a successful business with well-defined objectives and one that makes well-intentioned, but costly mistakes that puts the operation in financial risk.